

## Emerge Community Development

### Unity Opportunity Collaborative

Response to: Financial and Compliance Review and Investigation, Phase One, dated  
November 22, 2017

November 27, 2017

This memo represents Emerge's response to the Financial and Compliance Review and Investigation ("Review") conducted by Felton Financial Consultants, LLC on behalf of DEED and provided in draft form dated November 22, 2017.

We believe it is important to restate the environment in which the activities being reviewed were being conducted. The state legislator appropriated, in 2016, \$4.25 million to create a new community-led effort to provide workforce services to people of primarily African descent by a unique collaborative of six organizations. This bold new approach combined the unique strengths of each organization in a way that would overcome barriers that existed with traditional workforce practices and programs. The collaborative started on July 1<sup>st</sup> 2016 with a lot of discussion and learning amongst the group. Concurrently, DEED was given the responsibility to manage the appropriation which was outside of their normal way of doing business. Under these circumstances - ramping up a completely new program, it is not surprising that the actual contract between DEED and Emerge was not signed until September BUT was retroactive to July 1<sup>st</sup>, an acknowledgment by DEED that work providing direct services had started July 1. This initiative was new to all parties and there were challenges and learnings experienced by the collaborative and DEED alike. Again - this is not unexpected, and more importantly, through it all, a high level of service has been provided with results that, in most cases, will exceed initial goals.

EMERGE and its partners and its independent auditor conclude that the Review shows no malfeasance, no major accounting flaws, and highlights only minor recordkeeping details that have been corrected. Details for each finding are itemized below.

Most importantly, EMERGE and its subgrantees request that all activities and funding should be resumed immediately.

### **DETAILED RESPONSE TO THE REVIEW REPORT AND FINDINGS**

#### 1. Financial Review background clarification

The background described in the report provides a description and timeline of events and activities that occurred that gives an incomplete picture of the efforts put forth by Emerge to comply with the directives of DEED. Emerge did meet with DEED on September 1, 2017 where DEED described their concerns and outlined its expectations. This was followed up with a formal letter. Emerge did provide a robust response on September 11<sup>th</sup> as requested. In addition, Emerge reached out to DEED for clarification and guidance on several issues but did not receive a response. On September 29<sup>th</sup> DEED sent a list of 28 issues where further response

was required. Emerge responded as requested by October 6<sup>th</sup>, again in a robust manner and believing it had satisfied 21 of the 28 issues. The remaining issues were either in progress or awaiting discussion/clarification from DEED. Emerge received no response to any of its requests for clarification and discussion. In addition to the two detailed memos, cumulatively 35 exhibits were also provided in support of its responses. Emerge then received notice on October 16<sup>th</sup> that the present compliance review and investigation would begin on October 18<sup>th</sup>.

## 2. Results

We would like to highlight some important findings in the report and also some important facts that did not find their way into the report.

- The review found NO evidence of malfeasance - **Included**
- The auditor was able to tie the detailed financial records back to the audited financial statements - **Not Included**
- There were no findings for Minneapolis Urban League - **Included**
- There were no findings for StairStep Foundation - **Included**
- Cash advanced from DEED was managed appropriately - **Not Included**
  - o Total cash advanced from DEED was \$651K
  - o Total expense for the collaborative was \$899K
  - o Advanced cash was LESS than expense by \$248K
- Emerge distributed cash advances to its subs very quickly following the receipt from DEED. In two instances Emerge actually disbursed funds prior to its receipt from DEED - **Not Included**

Emerge Receipt Date from DEED	Emerge Disbursement Date to Subs
September 19, 2016	September 20, 2016
October 15, 2016	October 13, 2016
November 15, 2016	November 16, 2016
December 2, 2016	November 30, 2016
December 8, 2016	December 8, 2016

3. Emerge strongly disagrees with the contention that there are poor internal controls, undisciplined record keeping, poor understanding of adequate expense documentation and poor understanding of allowable expenses under the terms of this agreement.

- Many structures are in place at Emerge that contradict the statement made above.
  1. Emerge engages MACC (Metropolitan Alliance of Connected Communities) for much of its back-office operations including accounting services. MACC serves 50 plus non-profit organizations and is able to provide capacity, expertise, robust financial systems, segregation of duties and processes at a much higher level than small organizations could provide on their own. The controls and record keeping in place are VERY strong.

2. Emerge's long standing external auditor is Carpenter Evert, a well-respected firm that specializes in non-profit organizations. They conduct both a financial audit and a single audit each year and have always issued a clean opinion.
  3. Emerge has consistently met all standards of non-profit accountability for the Minnesota Charities Review Council and was recently reconfirmed
  4. Emerge successfully manages over 20 separate contracts valued in excess of \$7 million per year.
- The list of items identified as having inadequate documentation was small and never was there an instance of no documentation. It should be noted that where inadequate documentation only was cited there was not a contention that the expenses were invalid they simply could have had better support. A small number of instances of inadequate documentation does not equate to a poor understanding of adequate documentation.
  - The list of items deemed not allowable is even smaller and in many cases a good reason exists that invalidates the conclusion derived from a cursory review. We would strongly disagree that Emerge or its subs have a poor understanding of allowable expenses.

## 5. EMERGE Findings

Emerge had four findings. Each is addressed in detail below.

1. Emerge double-booked \$365,822 in UOC grants
  - o First of all, the term "double-booked" mischaracterizes the situation. Emerge recorded revenue and expense on its books for activity performed by itself and by its subcontractors. The independent third-party subcontractors recorded revenue and expense on their books for their activity. Each organization independently recorded their activity appropriately which is not "double-booking"
  - o As noted in the report, Emerge consulted with its external auditor as to the proper method to record the activity. It was determined that Emerge contracted with the subs to perform certain aspects of the programing for which Emerge was ultimately responsible for and, therefore, it was to be accounted for as an exchange transaction (revenue earned when expenses occur) rather than as a grant/contribution. This method dictates recording the revenue earned (from DEED) and expenses incurred (from subs) on its P&L
  - o If DEED had structured the contract where the subs were specified as secondary recipients then the accounting may be different. As it is structured, the subs are only mentioned as Emerge's explanation of the budget/workplan for the project and not secondary recipients. Emerge has the responsibility and authority to change, modify or cancel its agreement with the subs. This distinction dictated the accounting treatment. (exhibit 1 - External Auditor memo)

- o Emerge does not benefit from one accounting method or another and therefore its motivation is only to record the activity properly.
- o Emerge believes this a non-issue as it has no bearing the work performed or the requested reimbursement from DEED.
- 2. Circumvention of check signing limits
  - o Emerge acknowledges this situation occurred and it was a violation of our internal policy
  - o Please note the attached memo from our Board Vice-Chair and Finance and Operations Committee Chair (exhibit 2) noting their awareness that the pass-through payments would occur, they would have approved the payments and that we should have strictly adhered to the policy.
  - o This was done in good faith to expedite the payments to keep the collaborative operational and does not represent any type of pattern within the organization.
- 3. Lacked adequate support for UOC expenses
  - o In all instances where lack of documentation was noted, the invoice was present with the payment documentation but the support for the invoice was noted as insufficient by the auditor. In all cases, additional support existed but they were not with the invoices as they could have been. This has been corrected.
  - o Capable Communities – the billing did not coincide with the strict language in the contract. It is important to note that the issues were minor and the billing did align with the spirit of the agreement.
    - The contract has already been revised to align the spirit of the agreement with the actual contract language
      - Hours language was changed to be an average of 30 hours per week over the life of the contract. This allows some weeks to be higher and some to be lower.
      - Language was changed to allow more flexibility as to when billing occurs rather than strictly requiring billing every two weeks.
      - Language was added to allow invoicing of expenses but not mileage.
    - Willie Wallace – The contract did not mention reimbursement of expenses. This again was a minor issue that has been corrected. The contract has been revised to allow for expenses to be billed.
- 4. May exceed UOC administrative budget
  - o Emerge disagrees that this an issue at all as the budget category amount is a limit that cannot be exceeded. If Emerge chooses to spend more in this category it may do so but it simply will not be reimbursed.

## 6. Sabathani Findings

Sabathani had three findings.

- Lack of adequate support for expenses
- Disallowed expenses
- Non-UOC expenses

Sabathani had a total of eight expense items where one or more of the three findings was cited. Based on comments in the November 22<sup>nd</sup> meeting it appears that there are valid explanations that would make some of the expenses appropriate. Emerge will work with Sabathani to review each item to ensure the expenses are sufficiently substantiated. In the event that an expense is disallowed or non-UOC then these expenses will be adjusted out from any further reimbursement request.

## 7. CONCLUSION

This financial review has lasted more than a month, has put subgrantees in a highly vulnerable financial state as they provide services already started without payment. EMERGE cannot continue to serve as even a temporary funding source without assurances that DEED will compensate it for this activity. EMERGE and its subgrantees welcome the opportunity to continue to improve all related processes, but funding must be reinstated immediately to avoid irreparable harm. We are confident that all remaining issues can be successfully resolved and look forward to engaging with your staff in this process.